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BUREAU OF
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CURRENT
ANALYSES

(U) CHINA'S OPEN DOOR POLICY: NEW PRESSURES
AND OPPORTUNITIES

(S/NF) Summary

Despite continuing sensitivities within China over cultural contamination from the West, Deng Xiaoping and his reform-minded colleagues seem to be accelerating efforts to obtain foreign help for their ambitious modernization plans. When China first opened its doors to the West in the late 1970s, it was unsure of what to purchase and soon discovered that its economic health was still too precarious to sustain a major import program. Beijing's renewed interest in foreign imports and investment, particularly in recent months, is in part a reflection of China's overall economic recovery.

Recent years' experience, including the problems of industrial inefficiency and price reform, also may have given Chinese leaders a keener appreciation of the difficulty in overcoming the country's industrial backwardness without substantial help from the outside. Deng probably believes that the most difficult economic problems for China are technological and managerial and that the need to make progress in these areas justifies a step-up in purchases of advanced technology and related expertise.

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(C) Progress and Problems

Restraints on imports imposed in early 1981 were loosened in the final quarter of 1983, and China's imports rose 28 percent over the previous quarter. Imports for the year increased more than 10 percent after falling nearly 7 percent in 1982. Preliminary 1983 data indicate that industrial

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materials and capital goods accounted for the bulk of the increase in imports. China, last year, also increased its purchases of licenses and know-how. Chinese customs statistics suggest that this liberalized import policy is continuing. Imports during January-April were up nearly 20 percent compared with the same period last year. China is financially well positioned to afford the surge in purchases. Foreign exchange reserves amount to about \$16 billion.

While it has increased its direct purchase of foreign technology and capital goods, Beijing has attempted to accelerate foreign investments in China. China also is making greater efforts to enlist the help of overseas Chinese scientists and technical experts. Since mid-1983, China has initiated a number of measures to attract foreign interest including:

- a decision to allow technology firms to establish 100-percent-owned subsidiaries in China;
- a wider opening of its domestic market to goods produced by joint ventures;
- longer tax holidays for overseas investors;
- liberalized customs regulations for investors;
- new laws that will facilitate doing business in China; and
- permission to additional coastal cities to adapt concessionary policies to attract foreign investment.

Deng and his chosen successors committed themselves at the 1982 12th Party Congress to the goal of quadrupling China's industrial and agricultural output by the year 2000. This target has its exhortative role, but many Chinese planners and political leaders appear to have committed themselves to achieving such rapid growth. Their dedication, however, probably is tempered by recognition of formidable structural and institutional obstacles.

The increase in inflationary pressure resulting from initial steps to decentralize control over industry probably has added to Beijing's caution. Over the past two years, a too-rapid increase in heavy industry output strained energy supplies and transport services. Light industry production, meanwhile, grew slowly and failed to satisfy rising consumer demand. Investment also accelerated much too fast. Reform permitted enterprises to increase retained earnings, and enterprises used these funds to support new

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construction. Excess demand for steel, cement, and other construction materials slowed progress and raised costs on high-priority infrastructure projects.

Beijing earlier this year appeared to regain some of its control over the pace of investment by modifying rules governing project financing. Since late 1983, it also has managed to boost sharply production of consumer goods. Production costs, however, probably are continuing to rise, and gains in efficiency are not materializing. More far-reaching industrial reform is essential to eliminate noneconomic production and to increase productivity. Price reform, in particular, is critically needed to restore rationality in the price system.

Beijing is reluctant to speed the pace of reform because of its concern over inflation and its desire to minimize disruption of production and employment. Price reform is unlikely before 1985. Tax reform is scheduled for late this year, but it is not a good substitute.

The Risks

(S/NP/NC/OC) These problems have been crucial factors leading to the acceleration of China's open door policy. Although the opening to the West almost certainly has been a net political plus for the Dengists, it seems to have its detractors at senior levels. These opposition elements do not favor going back to the reclusive policy characteristic of the 1960s and early 1970s but object to the extent the Dengists have opened the door to foreign cultural influences. For the most part these elements are waging a rear-guard action, sniping from the sidelines and doing what little they can to circumscribe policy.

(S/NP/NC/OC) Beijing's drive late last year against "spiritual pollution" is the most recent in a series of efforts since 1979 to inoculate China against the undesirable side effects of Western influence. Unlike their predecessors, however, some influential Chinese went well beyond the limited targets of the campaign and launched an indirect but clear attack on Deng's economic open door policy. According to the Chinese press, these oppositionists criticized the importation of foreign technology and economic theories as well as the use of foreign management and scientific methods.

(S/NP/NC/OC) During the past few months, as the Dengists have regained the initiative and moved to circumscribe the anti-spiritual pollution drive, critics of the open door have been

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singled out for censure. Although it is difficult to determine the position of these oppositionists in the party hierarchy, the attention given to the problem in official documents suggests that the Dengists take them seriously.

(S/NF/NC/OC) The Special Economic Zones seem to be a sensitive facet of the open door policy. Deng and Premier Zhao Ziyang continue to exhibit a keen personal interest in dealing with problems in the zones, making frequent inspection tours. Since they were opened in 1979, the four zones appear to have made only a symbolic contribution to China's overall economic development while they have continued to feed charges by orthodox leaders that they serve as a conduit for negative foreign influences. To strengthen justification for the zones, the Dengists reportedly have made a recent decision to stress their function as a channel for Western technology and management know-how rather than as a major contributor to investment.

(C) The Deng camp appears willing to take the political risk involved in accelerating China's economic opening to the West because of the high stakes involved. Deng and his successors almost certainly recognize that the ability to develop a workable economic program that produces tangible results will be crucial to their political fortunes. Moreover, a good case can be made that Beijing's efforts to improve the political atmosphere with the US and Japan over the past year have been strongly influenced by the higher priority China has attached to the acquisition of foreign technology and expertise. In both instances, the Chinese have sought to downplay political problems and have gone to lengths to highlight the potential for expanded economic ties.

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